

Over the past month, I have received a number of emails concerning SFAS 141 (revised 2007), *Business Combinations*, and its testability on the CPA exam. Many astute CPA candidates have noted that they already need to be familiar with SFAS 141(R) for their audit work but are upset about seeing questions based on SFAS 141. Unfortunately, this is the nature of the beast known as the CPA exam.

New accounting and auditing pronouncements are eligible to be tested on the Uniform CPA Examination in the testing window beginning six months after a pronouncement's effective date. Some pronouncements are eligible for early application. When early application is permitted, the pronouncement may be tested in the window beginning six months after the issuance date. Thus, when either the old or the new pronouncement may be used by a practitioner, the side effect is that both are potentially testable on the CPA exam until the old pronouncement is superseded.

As noted above, we have received emails from sharp CPA candidates who inform us that we are teaching old information. They are usually correct, but the information in our books is what is being tested on the CPA exam due to the AICPA's aforementioned six-month (or longer) time lapse after the issuance date. I cannot promise that every CPA exam provider's materials are current, although I believe that most attempt to stay up-to-date. However, I can promise that Gleim materials are accurate in relation to what is being tested on the CPA exam.

SFAS 141(R) is effective for reporting periods beginning after December 15, 2008. Because early application is not permitted, it will not be testable on the CPA examination until the testing window beginning on July 1, 2009.

SFAS 141(R) applies the acquisition method of accounting and redefines a business combination as a transaction or event in which the acquirer obtains control of one or more businesses. The acquirer and acquisition date also are redefined in terms of who controls whom.

Moreover, SFAS 141(R) replaces the cost allocation method of accounting for a combination with the fair-value method. SFAS 141(R) measures assets acquired, liabilities assumed, and any noncontrolling interest at fair value at the acquisition date. Accordingly, goodwill is now measured as the excess of (1) the sum of the fair value of the consideration transferred, any noncontrolling interest, and any previously held equity in the acquiree over (2) the fair value of the identifiable net assets acquired. If (2) exceeds (1), the result (a bargain purchase) is recognized in earnings as an ordinary gain. Below is an example of the calculation of goodwill or gain:

EXAMPLE

Acquirer obtained 75% of the equity interests of Acquiree in a forced sale. Acquirer had no prior equity interest in Acquiree. Acquirer determined that the following are appropriate fair value measures to be used in accounting for this combination:

Consideration (\$300,000 of cash and \$250,000 of other assets) transferred by Acquirer	\$ 550,000
Acquirer's identifiable assets acquired	1,000,000
Acquiree's liabilities assumed	200,000
Noncontrolling interest in Acquiree	210,000

The gain is \$40,000 [(\$1,000,000 assets - \$200,000 liabilities) - \$550,000 consideration - \$210,000 noncontrolling interest].

The following entry is reflected in the worksheets used to prepare the acquirer's consolidated statements:

Identifiable assets	\$1,000,000
Cash	\$300,000
Other assets	250,000
Liabilities	200,000
Equity – noncontrolling interest (Acquiree)	210,000
Gain – bargain purchase	40,000

Another substantial change is that assets and liabilities arising from contractual contingencies are recognized at acquisition-date fair value. Noncontractual contingencies are recognized under SFAS 141(R) only if it is more likely than not that they meet the definition of an asset or a liability.

SFAS 141(R) is not the only new pronouncement testable in the July-August window. SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements*, has the same initial testing dates. SFAS 160

1. Requires that a noncontrolling interest be separately reported in equity
2. Requires that net income attributable to the parent and the noncontrolling interest be separately reported on the consolidated income statement
3. Provides new accounting rules for changes in the parent's ownership interest, including those resulting in deconsolidation

Below, I have provided an example of a consolidated income statement and an example of consolidated equity:

<u>EXAMPLE</u>	
Consolidated Income Statement	
Revenues	\$ XXX,XXX
Expenses	<u>(XXX,XXX)</u>
Pretax income from continuing operations	\$ XX,XXX
Income tax expense	<u>(XX,XXX)</u>
After-tax income from continuing operations	\$ XX,XXX
Discontinued operations (after tax)	<u>(X,XXX)</u>
Net income	\$ XX,XXX
Minus: Net income – noncontrolling interest	(X,XXX)
Net income – parent	<u><u>\$ XX,XXX</u></u>

<u>EXAMPLE</u>	
Consolidated Equity Section of Balance Sheet	
Equity:	
Parent equity:	
Common stock, \$1 par	\$XXX,XXX
Additional paid-in capital	XX,XXX
Retained earnings	XXX,XXX
Accumulated other comprehensive income	<u>XX,XXX</u>
Total parent equity	XXX,XXX
Noncontrolling interest	XX,XXX
Total equity	<u><u>\$XXX,XXX</u></u>

SFAS 162, *The Hierarchy of Generally Accepted Accounting Principles*, incorporates the nongovernmental GAAP hierarchy into a FASB pronouncement for the first time. Previously, this GAAP hierarchy was presented in Statement on Auditing Standards 69 (AU 411). SFAS 162 also adds additional sources of principles. SFAS 162 became effective in November 2008 and is therefore testable in July 2009. The following is a visual guide to the hierarchy (Level 1 is the highest):

Level 1

FASB Statements of Financial Accounting Standards and Interpretations, FASB Statement 133 Implementation Issues, FASB Staff Positions, and AICPA ARBs and APB Opinions.

Level 2

FASB Technical Bulletins and, if cleared by the FASB, AICPA Industry Audit and Accounting Guides and SOPS.

Level 3

AICPA Accounting Standards Executive Committee Practice Bulletins cleared by the FASB, consensus positions of the FASB Emerging Issues Task Force (EITF), and the Topics in Appendix D of *EITF Abstracts* (EITF D-Topics).

Level 4

Implementation guides (Q&As) published by the FASB staff, AICPA Accounting Interpretations, AICPA Industry Audit and Accounting Guides and SOPS not cleared by the FASB, and practices widely recognized and prevalent either generally or in the industry.

If a transaction or event is not specifically addressed in Levels 1-4, an entity considers whether a principle for a similar transaction or event applies. If not, the entity considers other accounting literature, for example, FASB Concepts and International Financial Reporting Standards (IFRSs).

The AICPA will not test the new FASB Codification in 2009 and they have not announced when they will begin testing the Codification. Relatedly, the AICPA has indicated that they will review and possibly revise their “six-month rule” regarding when new pronouncements will be tested. For the latest information about the CPA Exam, please visit our CPA Candidate Forum at <https://www.gleim.com/account/forum/cpa/index.php>.